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Chief, Industrial Division, OER

3 February 1959

THRU : Chief, Manufacturing Sectors Branch, D/I

Manufacturing Sectors Branch

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Comments on Draft SMIE 13-2-59.

REF : (a) CIA, ONE. SMIE 13-2-59: Present Trends in Communist China,
28 January 1959. S.

1. Reference (a) circulated a draft of SMIE 13-2-59, Present Trends in Communist China. This SMIE is scheduled for USIB consideration on 4 February. Research recently completed in the branch suggests the following comments which have been keyed to pages and paragraph numbers of reference (a). Although no specific OER contribution has been requested it is recommended that the Division forward these comments to ONE for their consideration.

2. Paragraphs 2, 3, and 6.

There appear to be certain contradictions in the draft with respect to Chinese experience in following the Soviet pattern of economic development. Paragraph 3 asserts that "in the years preceding 1958 the regime had apparently been doing very well by following the Soviet pattern of economic development based on modern heavy industry." Conceivably, the draft intends to draw a contrast between apparent success and discordant factors which had long been hidden to point up the fact that the explosive nature of the leap forward movement took the outside world by surprise. If so, the point seems a bit too subtle and may leave many readers somewhat confused when they read in paragraph 6, which analyzes motivations for the leap forward: "Dissatisfaction had also come from realization that the Soviet pattern of concentrating the nation's efforts almost entirely upon the development of heavy industry and the production of producer goods put excessive demands upon China's capital and technology, while slighting agriculture and the full use of China's massive manpower."

Moreover, the passage just quoted touches on only a few of the effects of slavish copying of the Soviets prior to 1958. Not only did the Chinese find it difficult to sustain the same pace in developing heavy industry and the production of producer goods, but they also discovered fundamental divergences in the pattern and methods of development.

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At the outset of the First Five-Year Plan the Chinese Communists placed complete faith in the applicability of the Soviet development model and technology to their own economic conditions. As a result, the growth of the Chinese machine-building industry was closely patterned after that of its Soviet counterpart. However, grave imbalances and dislocations appeared toward the end of the plan period which indicated to the Chinese not only that a number of objectives toward which the industry was progressing were unsuitable for Chinese economic conditions (e.g., agricultural mechanization) but also that the manner in which industrial construction projects were being carried out under Soviet plans had serious detrimental effects for Chinese economic growth as a whole, as discussed below. The resulting development was, consequently, unbalanced, extremely wasteful and excessively costly in terms of imported equipment. By 1958 the regime found it necessary to make drastic readjustments of production and investment priorities to support lagging agricultural growth and to revamp technological policy to harmonize with China's superabundance of labor. Many important features of Soviet experience have been discarded as the regime searches for a unique "Chinese" path of development, particularly in its emphasis on labor-intensive production in small- and medium-scale plants. Moreover, the Marxist predilection for economizing labor, virtually to the exclusion of other potential resource economies (e.g., land and capital), while reasonably well suited to the factor proportions prevailing in the USSR, has proved utterly incompatible with Chinese conditions. Thus, after only five years Soviet methods of forced industrialization on the basis of modern, large-scale industry had been tried in the Chinese context and had failed because they could not cope with Asia's fundamental problem -- too many people.

Before examining the results of Chinese Communist investment decisions in the machine building industry one theoretical point regarding the process of accumulation must be disposed of. Disregarding foreign aid for purposes of simplification, we may say that an economy which employs its resources fully must sacrifice a certain amount of consumption to provide accumulation for investment. However, where there is unemployment or underemployment of some resources, it is theoretically possible for investment and consumption to increase simultaneously. This maximization of production possibilities did not obtain in Communist China during 1953-57. Notable success was not achieved in eliminating underemployment in rural areas and also to a considerable extent in urban areas. Thus, in the Chinese context accumulation involved the increasing of output,

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mainly agricultural, the preventing of consumption from absorbing much of the increase, and the effective extraction of the surplus for the state. Somewhat oversimplified, the pattern of resource allocation would show a diversion of surplus agricultural production into export trade which were exchanged for capital goods for industrial investment.

Instead of allocating adequate resources for investment in quick-yielding projects, the Chinese concentrated almost entirely on slow-yielding investments in large-scale heavy industrial plants. This pattern of development had significant effects for the economy as a whole. As explained above, investment funds were accumulated through the sacrifice of consumption by the population. A lengthening of the period between the foregoing of consumption and the achievement of a higher level of production and income after the investment project is completed prolongs austerity. If full production is not then realized because of shortages due to insufficient investment in subsidiary or related industries, the expected relief to consumers through higher output and income will be further delayed. This would appear to be the case with the machine building industry in Communist China, where, for example, the 600 million yuan No 1 Motor Vehicle Plant operates at a fraction of its rated capacity because of insufficient supplies of critical materials.

A second effect of slow-yielding investments is a slower rise in industrial employment. By emphasizing modern, large-scale, capital-intensive plants, Chinese Communist industrial planners used the bulk of their scarce capital in investments which made relatively little use of the enormous supply of manpower in production, as distinguished from construction. There is evidence that higher employment could have been obtained by the investment of the same amount of capital in small- and medium-scale plants.

Third, as a consequence of the inability of the machine building and other industries to absorb the increase in manpower the Chinese economy experienced a slower rise in national income. The increase in national income could have been greater if newly created plants had been less capital-intensive. Although the state would have realized a lesser improvement in labor productivity per industrial worker than with larger concentrations of capital, a larger overall productivity gain would have resulted from the greater number of workers employed in industry. This follows from the markedly higher productivity of workers in industry as compared with those in agriculture.

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The slower pace of advance in national income correspondingly affects the ability of the state to extract accumulation for further investment by means of lowering the living standards of the rapidly expanding population. A Chinese writing in a Soviet economic journal in 1957 made the statement: "In such a country as China the most important factors for increasing social accumulation are maximal absorption of labor resources into production and the regime of the economy." Current plans for the machine-building industry emphasize increased inputs of labor.

Moreover, Chinese Communist investments in the machine-building industry were too widely diffused. This is explained, at least in part, by the fact that the Peiping regime followed Soviet experience too closely in pursuing the aim of self-sufficiency. They shared the intense Soviet zeal for economic independence from the West. They considered dependence on imports of capital goods from capitalist countries as a fundamental structural weakness in their economy which had to be eradicated as soon as possible. Indeed with the need for rapid improvement in the industrial support for national defense, the Chinese Communists emphasized a broad approach to the development of the machine-building industry. As a result the Chinese dispersed their investments in attempting to create simultaneously a number of new branches of the machine-building industry rather than concentrating on certain branches whose development would have contributed most to an intersectorally balanced economic growth.

3. Paragraphs 11-15, 13-21, Annex.

In analyzing the significance of the communes, particularly in their semi-industrial role, it should be emphasized that the regime seeks the solution to the problem of rural underemployment not only through better organization for tackling bigger mass-labor jobs, but also through what they describe as a "multiphased economy." In this diversified rural economy the commune functions to maximize productivity through a highly flexible allocation of labor that must be especially sensitive to the varying requirements of agriculture. Small-scale industries are to be set up in the countryside, but they are not intended to operate at a steady pace with a more or less fixed labor force. Production tempo will fluctuate sharply so as to maximize employment of labor in sideline occupations during the slack seasons while placing maximum labor resources at the disposal of agriculture during peak periods.

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4. Paragraph 16 and footnotes.

This branch takes very strong exception to the characterization of certain claimed output increases in machine building as "break throughs". Loose definition of what constitutes industrial machinery enables the Chinese Communists to exaggerate their output totals. For example, they recently announced production of 180,000 metric tons of metallurgical equipment in 1958. This claim is patently absurd, as this exceeds the Soviet level of output for 1957 and came in the midst of vigorous exhortations to overcome critical deficiencies in the production of rolling mill equipment. Obviously, a number of very crude items, associated with the hectic iron and steel smelting campaign, were counted in. Machine tools are another case in point. Peiping claimed that some 90,000 machine tools were manufactured in 1958. Significantly, however, it was admitted that only about half of these were produced in regular machine tool plants. The remainder, turned out in "native-style" shops and remarkable more for their ingenuity than for precision and durability, are hardly comparable with the genuine product.

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